Washington, DC -- Following news that large Wall Street banks plan to sidestep new rules designed to prevent another Wall Street Meltdown, Congressman Maurice Hinchey (D-NY) joined by nine other members of the U.S. House, is urging the Federal Reserve to prevent banks from avoiding the new regulation. A provision of the Dodd- Frank Wall Street Reform bill, called the Volcker Rule, was intended to prevent commercial banks from engaging in proprietary trading, whereby federally insured deposits are used for risky trades. It has been widely reported that banks plan to skirt the rule by redefining proprietary trading to exclude so called "principal investments."

"We cannot allow Wall Street to get around the law designed to prevent another Wall Street meltdown," said Hinchey. "Banks may want to get around the rule and pretend that depositors money isn't being dumped into Wall Street's communal slot machine, but the plain fact is that the Fed determines and defines what proprietary trading is - not the big banks. Congress gave the Federal Reserve the authority to clamp down on risky trades and now they need to use it. The health of our economy depends on it."

In the wake of the Great Depression, Congress passed the Banking Act of 1933, which became known as the Glass-Steagall Act, to wall off interaction between the commercial and banking sectors. For the next 60 years the U.S. enjoyed long periods of growth with minimal exposure to risk. In 1999 however, Congress repealed the Glass-Steagall reforms by passing the Gramm Leach Bliley Act which removed the separation between the commercial and banking sectors, contributing to the economic crisis in 2008. Last year, Congress again instituted a measure to govern the separation between these two sectors in the form of the Volcker Rule - the provision which banks are now attempting to sidestep.

In their letter, the House members asked the Federal Reserve to define the Volcker Rule so it limits proprietary trading in all respects, including long term bets which may be categorized as "principal investments." The Dodd Frank Wall Street Reform law, which Hinchey supported, gives Federal Reserve flexibility in implementing the rule. The full text of the letter follows. A PDF can be found here.

June 07, 2011

The Honorable Ben S. Bernanke, Chairman

Board of Governors for the Federal Reserve System
20th Street and Constitution Avenue, Northwest
Washington, D.C. 20551

Dear Chairman Bernanke:

As the Federal Reserve continues its work to implement the major provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, we encourage the Federal Reserve to take particular care when defining the Volcker Rule. Recent news reports indicate some bank holding companies anticipate that long-term "principal investments" will not be considered proprietary trading under the Volcker Rule. The Federal Reserve needs to correct this assumption by including both short-term and long-term trades in its definition of proprietary trading. When a commercial bank engages in proprietary trading for its own profits, customer's federally insured banking deposits are exposed to significant additional risk. The Volcker Rule can minimize this risk by limiting the investment activities that can be conducted by commercial banks, which is essential to a healthy and stable U.S. economy.

In 1929, an unregulated banking sector led to a Wall Street crash that devastated the economy. To ensure such a catastrophic event would not be repeated, Congress passed the Banking Act of 1933, which put in place a new regulatory framework for the banking sector. This legislation included an important provision that walled off interaction between the commercial and banking sectors, which became informally known as the Glass-Steagall Act. For the next 60 years, the U.S. enjoyed long periods of growth with minimal exposure to risk. Unfortunately in 1999, Congress passed the Gramm Leach Bliley Act which removed this important separation between commercial and investment banking and paved the way for Wall Street to, once again, run amok.

In 2008, less than a decade after Glass Steagall was repealed, we experienced an economic crisis second only to the Great Depression. Deregulation of Wall Street emboldened megabanks to become highly leveraged and take excessive risks with federally insured banking deposits. In addition, we saw the creation of large bank holding companies that housed a range of banking activities, including commercial banking, investment banking and insurance. These entities grew in such excess that their failure posed systemic risk to the U. S. economy. One again, Congress was moved to respond to an unregulated Wall Street. Congress moved to bailout major bank holding companies including JPMorgan Chase, Bank of America, Wells Fargo and Citigroup. These four banks held roughly 40 percent of America's bank deposits. Had these commercial banking institutions been limited in their investment banking activities initially, it is likely that we would have avoided an economic situation where the American people were held hostage by a mammoth financial industry. It is with great urgency that we must bring back the regulations that separate the investment and commercial banking sector.

The financial reform legislation recently passed by the Congress, granted the Federal Reserve Board the authority to adopt additional rules regarding the definition of the Volcker Rule. Specifically, the Federal Reserve should define the Volcker Rule so it limits proprietary trading in all respects, including long term bets which may be categorized as "principal investments." By including long term "principal investments" in the definition of the Volcker Rule, you are truly upholding the intent of the Volcker Rule and the Glass Steagall Act. News reports confirm that many large financial institutions will continue to engage in long-term proprietary trading unless it is specifically included in the Volcker Rule definition. As the Federal Reserve moves to issue these proposed rules, we request that the Federal Reserve hold up the spirit of the Volcker Rule.

Sincerely,

Rep. Maurice D. Hinchey
Rep. John Conyers Jr.
Rep. Marcy Kaptur
Rep. Louise M. Slaughter
Rep. Bob Filner
Rep. Peter DeFazio
Rep. Jan Schakowsky
Rep. Pete Visclosky
Rep. Peter Welch
Rep. Earl Blumenauer